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IN THE

Supreme Court of the United States

OCTOBER TERM, 1940.

No. 2.

NEW WORLD LIFE INSURANCE CO., *Petitioner,*

v.

THE UNITED STATES.

On Writ of Certiorari to the Court of Claims.

PETITIONER'S REPLY BRIEF.

PRELIMINARY.

The respondent raises for the second time in his brief the question of whether the writ of certiorari herein should be dismissed, which was previously raised in respondent's motion to dismiss the writ. This motion this Court denied on October 14, 1940.

Petitioner's reply brief will discuss the question referred to above, as well as certain other contentions made by respondent, particularly its request that this Court reconsider its decision in *Helvering* v. *Reynolds Tobacco Co.*, 306 U. S. 310.

STATEMENT.

On September 24, 1940, respondent filed a motion in this Honorable Court to dismiss the writ of certiorari, on the ground that the question presented by the writ was moot. On September 30, 1940, the petitioner filed a brief in opposition to respondent's motion to dismiss the writ. In addition to the facts stated in respondent's said motion, the petitioner showed that it had another suit pending in the Court of Claims, *New World Life Insurance Company* v. *U. S.*, No. 44580, involving the question of whether petitioner is entitled to deductions of $5,376.90 and $5,417.88 for the years 1933 and 1934, respectively, representing 3¾ per cent of the mean of its Disabled Lives Reserves, an identical question now presented by the present writ, and that the dismissal of the writ would result in compelling the petitioner and the respondent to litigate the same question anew in the Court of Claims, a procedure expensive to the petitioner and to the Government, as well as an unnecessary burden upon the Court of Claims and this Honorable Court. (Pet. Br. in Opp., 2, 3.)

At the time of filing petitioner's said brief in opposition to the granting of the respondent's said motion to dismiss the writ on September 30, 1940, petitioner filed a "Motion for Leave to File Waiver of Statute of Limitations and Consent to Judgment" for the year 1931; and petitioner attached to its said motion a duly executed "Waiver of Statute of Limitations and Consent to Judgment" for the year 1931. (Pet. Br. in Opp., 6-9.)

This Honorable Court did not pass upon petitioner's said motion for leave to file said waiver and consent to judgment, and petitioner is not clear as to whether this Court gave any consideration to the same. Petitioner submits, however, that it had the unqualified right to file said Waiver of Statute of Limitations and Consent to Judgment without leave of this Court (37 *C. J.* 721); and that petitioner's said Waiver of Statute of Limitations and Consent to Judgment for the year 1931 was properly filed in this Court on September 30, 1940.

The Commissioner's Regulations from 1921 to 1935 authorized a life insurance company to take a deduction of the statutory percentage of the mean of the Active Lives Reserve and of the Disabled Lives Reserve. Furthermore, Form 1120-L (corporate life insurance income tax return for the years 1921 to 1932, prepared by the Commissioner) contained lines for said deduction.

On February 11, 1935 the Commissioner, with the approval of the Secretary of the Treasury promulgated Reg. 86, Art. 203 (a) (2)-1 under the Revenue Act of 1934, in which he omitted the authorization for the deduction in respect of Active Lives Reserves and Disabled Lives Reserves but did not specifically deny said deductions, with the exception that said regulations specifically stated that reserves held on account of waiver of premiums were not reserve funds required by law within the meaning of the Revenue Act of 1934.

It was not until December 18, 1935, that the Commissioner promulgated T. D. 4615, amending Art. 681 of Reg. 62, 65, and 69, applicable to the Revenue Acts of 1921, 1924, and 1926, respectively, and Art. 971 of Reg. 74 and 77, applicable to the Revenue Acts of 1928 and 1932, respectively, so that these regulations would conform to Art. 203 (a) (2)-1 of Reg. 86.

Art. 681 of Reg. 62, 65, and 69, Art. 971 of Reg. 74 and 77 as originally promulgated and as amended, as well as Art. 203 (a) (2)-1 of Reg. 86 (1934 Act), Art. 203 (a) (2)-1 of Reg. 94 (1936 Act), and Art. 203 (a) (2)-1 of Reg. 101 (1938 Act) contained a specific authorization for a deduction with respect to disability reserves *not required by law* in the case of life insurance companies issuing policies covering life, health, and accident insurance combined in one policy issued on the weekly premium payment plan, continuing for life and not subject to cancellation. (Appendix, p. 21.) For some reason respondent saw fit to omit this provision of the regulations. (Appendix, Resp. Br. 56.)

ARGUMENT.

I.

The Respondent is Precluded From Raising the Moot Question Issue Again at This Time.

The question is res judicata.

No new facts have been presented by the respondent in its brief which were not set out in its original motion to dismiss the writ and in the petitioner's brief in opposition. It is submitted that the question is *res judicata*, and particularly that the respondent is not entitled at this time to reopen the question without a showing of new material facts which were not available to respondent at the time its original motion was filed.

In *Patterson* v. *Ford*, 8 Pac. (2d) 1006, 167 Wash. 121, the Supreme Court of the State of Washington held that where a respondent filed a motion to dismiss an appeal on the ground that it was defective and later renewed its motion on the same ground, the question was *res judicata*. We quote as follows:

> "Respondents move that the appeal be dismissed upon the ground that the bond on appeal is not in compliance with the requirements of section 1722, Rem. Comp. Stat.
>
> "This is a renewal of respondents' motion which was heard in this court and denied September 25, 1931. The matter is now *res judicata*."

In *H. L. Doherty & Company* v. *Youngblut*, 185 Pac. 257, 66 Colo. 594, the Supreme Court of Colorado on the question of a second motion to dismiss held as follows:

> "The defendants in error move to dismiss on several grounds. The plaintiffs in error answer that defendants in error cannot do this, because they have already moved and failed, and the present grounds were available at the time of the former motion, and plaintiffs in error call attention to the fact that since the former

motion they have expended large sums in the preparation and printing of abstracts and briefs.

* * * * * * * * *

"We think the position of plaintiffs in error is sound.

* * * * * * * * *

"The motion to dismiss is denied."

In *Bisbee* v. *Whitmore*, 241 N. W. 162, 257 Mich. 178, a supplemental brief was filed asking reconsideration of a previous motion to dismiss the appeal, and the court declining to do so said:

> "After this case was submitted to this court, plaintiffs filed a 'supplemental brief,' asking reconsideration of their motion to dismiss the appeal, which was denied January 5, 1931. Reconsideration, if desired, must be timely moved. No new reasons are alleged nor points other than those we then passed upon are submitted. We decline to reconsider our former adjudication."

On the same question the Court of Appeals of Illinois in *Elliott, Administrator* v. *Trandel*, 277 Ill. App. 359, after denying a first motion, declined to grant a second motion to dismiss an appeal. We quote:

> "In support of the judgment appealed from, the plaintiff contends that the bill of exceptions should be stricken from the record and the appeal dismissed. The plaintiff has previously made a motion to that effect in this court and on December 13, 1921, the motion was denied. It will, therefore, not again be considered at this time."

The Rules of This Court Bar Reconsideration of the Questions Raised in Respondent's Motion.

Paragraph 3 of Rule 7 of this Court, provides

> "A motion by respondent to dismiss a writ of certiorari or by appellee to dismiss an appeal after the court has ruled upon the jurisdictional statements and accompanying motions, if any (Rule 12, par. 5), will be re-

> ceived if not *based upon grounds already advanced in opposition to the granting of the writ of certiorari or to the noting of jurisdiction of the appeal.*"

If a respondent be not permitted to file a motion to dismiss a writ of certiorari, after he has already advanced the same grounds in opposition to the granting of the writ, *a priori*, the respondent in this case should not be permitted to reopen the identical question, which was presented in respondent's original motion to dismiss the writ and, which was considered by this Court in denying the respondent's said motion.

Presumably, the respondent will attempt to argue the question of whether the issue presented by the writ is moot, which will be in violation of Paragraph 2 of Rule 7 of this Court, which reads:

> "Oral argument will not be heard on any motion unless the court specially assigns it therefor, when not exceeding one-half hour on each side will be allowed."

If the respondent desired the Court to reconsider its original motion to dismiss, the respondent should have filed a petition for a rehearing within twenty-five days after October 14, 1940, as provided in Rule 33; and even that rule, which reads as follows, does not permit oral argument:

> "Such a petition is not subject to oral argument, and will not be granted, unless a justice who concurred in the judgment desires it, and a majority of the court so determines."

Authorities Cited by Respondent Do Not Support Its Contention.

Respondent cites *California* v. *San Pablo & C. Ry. Co.*, 149 U. S. 308, as authority for the proposition that the pendency of other cases does not justify this Court's retention of a case in which a moot question is involved. (Resp. Br. 17.) That case, however, is one in which entirely different

parties in entirely different suits had stipulated that said other cases should abide the decision of the Supreme Court in the case at bar. This Court declined to decide the case on the merits because the question was moot, and dismissed the writ of error. That is entirely different from a situation such as the instant one, in which the identical parties have an identical question pending in another suit in the identical courts; viz., the Court of Claims and the Supreme Court.

Respondent argues that this Court is precluded from deciding the instant case on the merits on account of the Declaratory Judgments Act, which is inapplicable to Federal Taxes. (Resp. Br. 16.) That Act, of course, does not apply here, inasmuch as no suit was instituted by petitioner in the Court of Claims for a declaratory judgment. In the event that this Court decides the instant case on the merits, its decision will be binding on the petitioner and the respondent in the other case pending in the Court of Claims.

II.

The Filing of Waiver of Statute of Limitations and Consent to Judgment Sufficed to Keep the Question Alive at All Events.

As pointed out in petitioner's brief in opposition to respondent's motion to dismiss the writ, the question presented by the writ did not become moot, if at all, until this Court denied the petition for a writ of certiorari with respect to investment expenses on May 20, 1940.

On September 30, 1940, petitioner filed in this Court a Waiver of Statute of Limitations and Consent to Judgment for 1931. Clearly the filing of petitioner's said Waiver of Statute of Limitations and Consent to Judgment for 1931 is sufficient to keep the question alive for 1931, if this Court should decide that the pendency of the other suit in the Court of Claims alone is insufficient for that purpose. (37 C. J. 721.)

Petitioner submits, therefore, that respondent is precluded at this time from renewing its motion to dismiss the writ; and that the question presented by the writ is not moot, because there is pending another case in the Court of Claims, and there is on file in this Court a Waiver of Statute of Limitations and Consent to Judgment for 1931.

If, however, the Court should dismiss the writ, petitioner respectfully asks the Court to reverse the Court of Claims on the reserve fund question in accordance with the usual practice of this Court. (*Leader* v. *Apex Hosiery Co.*, 302 U. S. 656; *Woodring* v. *Clarksburg Bridge Company*, 302 U. S. 658; *Alejandrino* v. *Quezon*, 271 U. S. 528; *Broconlow* v. *Schwartz*, 261 U. S. 216, 218; *Heitmuller* v. *Stokes*, 256 U. S. 359; *Commercial Cable Co.* v. *Burleson*, 250 U. S. 360; *Public Utilities Comrs.* v. *Compania General de Tabacos*, 249 U. S. 425; *Berry* v. *Davis*, 242 U. S. 468, 470; *U. S.* v. *Hamburg Amerikanische Co.*, 239 U. S. 466.)

III.

Granting Petitioner a Deduction in Respect to Its Disability Reserves Does Not Favor Petitioner Over Other Classes of Insurance Companies.

Respondent contends that the statute accords a life insurance company "unusually favorable treatment" (Resp. Br. 21); that the deduction of the statutory percentage of the mean of reserve funds gives a life insurance company "a unique deduction of unusual magnitude" (Resp. Br. 22); and that to permit a life insurance company to take a deduction in respect of its disability reserves would favor such a company over other classes of insurance companies, inasmuch as no such deduction is available to them. (Resp. Br. 23, 29.) At another place respondent refers to this deduction as a "windfall" to insurance companies. (Resp. Br. 47.)

Petitioner respectfully submits that the foregoing statements of the respondent are based upon a misapprehension

of the general scheme of taxation which Congress provided for the various classes of insurance companies; that other insurance companies receive the equivalent of the deduction of the statutory percentage of the mean of reserve funds given to a life insurance company; and that to deny a life insurance company a deduction in respect of disability reserves in fact would discriminate aginst such a company in favor of other classes of insurance companies.

Congress provided for the taxation of insurance companies according to three different classifications; viz.,

(1) "Tax on life insurance companies," (Secs. 201-203);

(2) "Tax on insurance companies other than life or mutual," (Sec. 204);

(3) "Tax on mutual insurance companies other than life."[1] (Sec. 208.)

Under this scheme of taxation, these three classes of insurance companies are taxed as follows:

"Life insurance companies" include in gross income only income received from investments, such as dividends, interest and rents, excluding therefrom premium receipts. (Sec. 202 (a).) They are not allowed any deduction for amounts actually paid to policyholders in satisfaction of claims; but life insurance companies are allowed a deduction of an amount equal to 3¾% or 4% of the mean of reserve funds required by law, which reserve funds are set up for the purpose of ultimately paying claims under their policies when they mature. (Sec. 203 (a) (2).) "Life insurance companies," therefore, are not taxed on premium receipts or on that portion of investment income added to reserve funds maintained to pay policyholders' claims when they mature.

Insurance companies "other than life or mutual" include in gross income, investment income and premiums earned. (Sec. 204 (b) (1)-(5).) They are allowed deductions for

[1] See Appendix, Respondent's brief, for the statutes applicable to the foregoing classes of insurance companies.

"losses incurred;" *i.e.*, losses actually paid to policyholders in satisfaction of claims. (Sec. 204 (b) (6).) "Insurance companies other than life or mutual," therefore, are not taxed on that portion of premium receipts or investment income used to pay policyholders' claims.

"Mutual insurance companies other than life" include in gross income, investment income, premium receipts, and all other classes of income. (Sec. 208 (a).) They are allowed to deduct amounts actually paid to policyholders in satisfaction of claims (Sec. 208 (c)), and also "the net addition required by law to be made to reserve funds" (Sec. 208 (c) (1) (A).), as well as certain other deductions. "Mutual insurance companies other than life," therefore, are not taxed on that portion of premium receipts, or on that portion of investment income, which is actually paid in satisfaction of policyholders' claims.

Thus it will be seen that under each of the three plans of taxing insurance companies, Congress has not taxed any class of insurance companies on that portion of premium receipts, or on that portion of investment income, which currently or ultimately is used to satisfy policyholders' claims. The method of accomplishing this varies; but the result is the same. For instance, life insurance companies get their deduction from gross income at the time the amounts are *set aside* in reserve funds, which ultimately are to be used to pay policyholders' claims; whereas, insurance companies other than life or mutual and mutual insurance companies other than life get their deduction when the losses are actually paid.

Hence it is clear that if petitioner were to be denied a deduction of the statutory percentage of its active Lives and Disabled Lives Reserves, which amounts ultimately are used to pay disability claims arising under its policies of combined life, health and accident insurance, instead of being favored, as argued by respondent, petitioner would be discriminated against as compared with other insurance companies, inasmuch as such other insurance companies

would receive the equivalent of such deduction at the time they paid their policyholders' claims, whereas petitioner would not receive any deduction either at the time the amounts were set aside in reserve funds or at the time the claims actually were paid.

From the foregoing, it is apparent that there is no basis for respondent's statement that the reserve deduction given to life insurance companies is "a unique deduction of unusual magnitude," or a "windfall" deduction, or that such deduction favors life insurance companies over other kinds of insurance companies.

IV.

Colloquy Between a Senator and Treasury Representative Not Admissible.

Respondent refers to a certain colloquy between Senator McCumber and Dr. Adams at the time the Revenue Act of 1921 was under consideration as evidence of the congressional intent that health and accident insurance reserves held in respect of policies of *combined* life, health and accident insurance should not be combined with life insurance reserves for the purpose of determining whether an insurance company is a life insurance company within the meaning of Sec. 201(a). (Resp. Br. 25-26.) Even though the interpretation placed upon this colloquy by respondent is correct, nevertheless this Court will not resort to such evidence for the purpose of construing an Act of Congress, as it has been held repeatedly that resort may not be had even to debates of Congress in connection with a bill at the time it is under consideration. (*United States* v. *St. Paul, M. & M. R. Co.*, 247 U. S. 310, 62 Law Ed. 1130; *Standard Oil Co.* v. *United States*, 221 U. S. 1, 55 Law Ed. 619; *Omaha & C. B. Street R. Co.* v. *Interstate Commerce Commission*, 230 U. S. 324, 57 Law Ed. 1501; *Lapina* v. *Williams*, 232 U. S. 78, 58 Law Ed. 515; *McCaughn* v. *Hershey Chocolate Co.*, 283 U. S. 488, 75 Law Ed. 1183; *Humphrey* v. *United States*, 295 U. S. 602, 79 Law Ed. 1611.)

V.

Helvering v. Reynolds Tobacco Co., 306 U. S. 310, Correctly States the Rules Regarding Retroactive Regulations.

Respondent argues feebly that the application of the amended regulations is not prohibited by the decision of this Court in the *Reynolds Tobacco* case. By requesting this Court to reconsider its decision in that case, the respondent tacitly admits that the Commissioner is prohibited from applying his amended regulations to taxable years prior to 1934.[1] (Resp. Br. 37.)

This Court held in the *Reynolds Tobacco* case that where the statute is so general in terms as to render an interpretative regulation appropriate, and Congress has repeatedly reenacted the statute without change, the Commissioner may not amend his regulations and apply them retroactively except to correct misinterpretations, inaccuracies, or omissions in the existing regulations.

Respondent now argues that the Treasury has "*full and complete discretion* to determine to what extent changes in regulations are to operate retroactively" (Resp. Br. 45), and that in the event that the *Reynolds Tobacco* case be deemed to be in conflict with this theory, that case should be overruled. (Resp. Br. 47.)

Petitioner respectfully submits that the decision of this Court in that case lays down a sound rule, which is equitable to the government and to taxpayers and that Congress did not intend to give to the Treasury Department the absolute power to change regulations at will and to apply them arbitrarily to past years irrespective of prior administrative practice.

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[1] The only basis for respondent's contention that the *Reynold's Tobacco* case does not prohibit him from applying his amended regulations retroactively is that the original regulations did not correctly interpret the statute. That the prior regulations correctly interpreted the statute, we demonstrated in our original brief. Also see respondent's brief in *Com.* v. *Pan American Life Ins. Co.*, No. 264, p. 19, for a logical discussion of the correctness of this decision.

This Court has held repeatedly that reenactment of a statute by the Congress without change must be taken as approval by Congress of the administrative construction and thereby to give such construction the force of law.

The Commissioner's Regulations for fourteen years provided that a life insurance company was entitled to a deduction in respect of disability reserves. During this period of time Congress reenacted the law unchanged five different times after the first enactment in 1921. The Commissioner's regulations from 1921 to 1935, therefore, must be recognized as having the force of law. If respondent's argument were sound, the Commissioner had the authority in 1935 to change his prior regulations so as to deny a deduction in respect of disability reserves, a deduction which his prior regulations held was permissible—in effect the Commissioner had the authority to repeal the prior regulations and promulgate new ones, and *a priori*, the authority to repeal the statute itself and enact a new one. Respondent cites certain statutes as authority for the proposition that the Treasury Department has full and complete discretion to apply regulations retroactively as he sees fit. This Court in the *Reynolds Tobacco* case considered Sec. 605 of the Revenue Act of 1928, cited by the respondent (Resp. Br. 43), and held

> "that Congress intended to give to the Treasury power *to correct misinterpretations, inaccuracies, or omissions* in the regulations, and thereby to affect cases in which the taxpayer's liability had not been finally determined, unless in the judgment of the Treasury, some good reason required that such alterations operate only prospectively. The question is whether the granted power may be exercised in an instance where, by repeated reenactment of the statute, Congress has given its sanction to the existing regulation.
>
> "Since the legislative approval of existing regulations by reenactment of the statutory provision to which they appertain gives such regulations the force of law, we think that Congress did not intend to au-

thorize the Treasury to repeal the rule of law that existed during the period for which the tax is imposed."

Respondent argues that Congress has gradually increased the Commissioner's power until it is complete. Instead of Congress gradually increasing the power of the Commissioner until his power is "complete," as argued by the respondent, petitioner respectfully submits that Congress gradually curtailed the Commissioner's power in respect of retroactive regulations.

For instance, Sec. 1314 of the Revenue Act of 1921 gave the Commissioner power to apply a new regulation without retroactive effect, where such new regulation *reversed* a prior regulation. This same provision was carried forward into the Revenue Acts of 1924 and 1926. (Resp. Br. 39-41.) A decided reduction in the Commissioner's power, however, was made in Sec. 605 of the Revenue Act of 1928, in that his power was restricted to regulations which *amended* prior regulations. Beginning in 1928, therefore, the Commissioner no longer had power to decide whether a regulation *reversing*[1] a prior regulation should have retroactive effect. Thereafter, as this Court held in construing Sec. 605, *supra*, the Commissioner's power in respect of retroactive regulations was limited to those which corrected "misinterpretations, inaccuracies, or omissions" (*Helvering* v. *Reynolds Tobacco Co., supra*); that is to which *amended* prior regulations.

---

[1] To reverse means:

"To turn in opposite directions; * * * alter to the opposite in character or tendency, or change completely; * * * also to revoke, repeal or annul. * * *" (The New Century Dictionary, p. 1547.)

Whereas to amend means:

"To remove or correct faults in; changes for the better. * * *" (Id., p. 38.)

The committee report (Resp. Br. 44) shows that Congress did not in enacting Sec. 506 of the Revenue Act of 1934 (Resp. Br. 43) intend to restore to the Commissioner authority with respect to regulations which *reversed* prior regulations, but on the other hand to continue the same power relative to regulations *amending* prior regulations and also to extend the Commissioner's power to regulations which did not amend prior regulations; *i. e.*, entirely new regulations.

To summarize, the Commissioner had no statutory power in 1935 to *reverse* his prior regulations applicable to the Revenue Acts of 1928 and 1932 and prior revenue acts and to apply such revised regulations retroactively to taxable years prior to the time the reversal was made as the respondent is attempting to do in the instant case. The *Reynolds Tobacco* case was correctly decided and that decision should be held to apply to the instant case.

The construction contended for by the respondent would amount to an abdication or transfer to an administrative officer of essential legislative functions, which this Court in *Schechter* v. *U. S.*, 295 U. S. 495, 529, held that Congress could not do; and if the sections cited by the respondent be susceptible of such construction, they are unconstitutional as an unwarranted delegation of legislative power.

CONCLUSION.

It is respectfully submitted that the decision of the Court of Claims should be reversed.

Respectfully submitted,

WALTER E. BARTON,
Counsel for Petitioner.

APPENDIX.

House Revenue Bill of 1921.

TAXES ON INSURANCE COMPANIES.

Sec. 242. That when used in this title the term "life insurance company" means an insurance company engaged in the business of issuing life insurance and annuity contract* (including contracts of combined life, health, and accident insurance), the reserve funds of which held for the fulfillment of such contracts comprise more than 50 per centum of its total reserve funds.

Sec. 243. That in lieu of the taxes imposed by sections 230 and 1000 there shall be levied, collected, and paid for the calendar year 1922 and for each taxable year thereafter upon the net income of every insurance company a tax as follows:

(1) In the case of a domestic insurance company, 12½ per centum of its net income;

(2) In the case of a foreign insurance company, 12½ per centum of its net income from sources within the United States.

Sec. 244. (a) That in the case of an insurance company the term "gross income" means the gross amount of income received during the taxable year from interest, dividends, and rents.

(b) The term "reserve funds required by law" includes, in the case of assessment insurance, sums actually deposited by any company or association with State or Territorial officers pursuant to law as guaranty or reserve funds, and any funds maintained under the charter or articles of incorporation of the company or association exclusively for the payment of claims arising under certificates of membership or policies issued upon the assessment plan and not subject to any other use.

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* The word was pluralized in the bill as finally passed.

Sec. 245 (a). That in the case of an insurance company the term "net income" means the gross income less—

(1) The amount of interest received during the taxable year which under paragraph (4) of subdivision (b) of section 213 is exempt from taxation under this title;

(2) An amount equal to the excess, if any, over the deduction specified in paragraph (1) of this subdivision, of 4 per centum of the mean of the reserve funds required by law and held at the beginning and end of the taxable year, plus (in case of life insurance companies issuing policies covering life, health, and accident insurance combined in one policy issued on the weekly premium payment plan, continuing for life and not subject to cancellation) 4 per centum of the mean of such reserve funds (not required by law) held at the beginning and end of the taxable year, as the Commissioner finds to be necessary for the protection of the holders of such policies only;

(3) The amount of dividends included in the gross income;

(4) In the case of life insurance companies, an amount equal to 2 per centum of any sums held at the end of the taxable year as a reserve for dividends (other than dividends payable during the year following the taxable year) the payment of which is deferred for a period of not less than five years from the date of the policy contract;

(5) Investment expenses paid during the taxable year: *Provided,* That if any general expenses are in part assigned to or included in the investment expenses, the total deduction under this paragraph shall not exceed one-fourth of 1 per centum of the book value of the mean of the invested assets held at the beginning and end of the taxable year;

(6) Taxes and other expenses paid during the taxable year exclusively upon or with respect to the real estate owned by the company, not including taxes assessed against local benefits of a kind tending to increase the value of the

property assessed, and not including any amount paid out for new buildings, or for permanent improvements or betterments made to increase the value of any property;

(7) A reasonable allowance for the exhaustion, wear and tear of property, including a reasonable allowance for obsolescence;

(8) All interest paid within the taxable year on its indebtedness, except on indebtedness incurred or continued to purchase or carry obligations or securities, the interest upon which is wholly exempt from taxation under this title as income to the taxpayer.

Regulations.

Art. 971 of Reg. 74 (1928 Act) and Art. 971 of Reg. 77 (1932 Act) prior to amendment, as hereinafter referred to, were the same and read as follows:

"Under paragraphs (1) and (2) of section 203 (a), life insurance companies are entitled to deduct from gross income:

"(1) Interest which is exempted in the case of other taxpayers by section 22 (b) (4) and articles 84-87;* and

"(2) Four per cent of the mean of the reserve funds required by law and held at the beginning and end of the taxable year, except that in the case of any such reserve fund which is computed at a lower interest assumption rate, the rate of 3¾ per cent shall be substituted for 4 per cent. The reserve deduction is based upon the reserves required by express statutory provisions or by the rules and regulations of the State insurance departments when promulgated in the exercise of a power conferred by statute; but such reserves do not include assets required to be held for the ordinary running expenses of the business nor do they include the reserve or net value of risks reinsured in other solvent companies to the extent of the reinsurance.

* 88 in Art. 971 of Reg. 74.

"In the case of life insurance companies issuing policies covering life, health, and accident insurance combined in one policy issued on the weekly premium payment plan, continuing for life and not subject to cancellation, it is required that reserve funds thereon be based upon recognized tables of experience covering disability benefits of the kind contained in policies issued by this particular class of companies.* The deduction in respect of such reserve funds (not required by law) is 3¾ per cent of the mean of such reserve funds held at the beginning and end of the taxable year. Reserves maintained to provide for the ordinary running expenses of a business, definite in amount, and which must be currently paid by every company from its income if its business is to continue, such as taxes, salaries, reinsurance, and unpaid brokerage will not be considered. A company is permitted to make use of the highest aggregate reserve called for by any State in which it transacts business, but the reserve must have been actually held as shown by the annual Statement. Generally speaking, the following will be considered reserves as contemplated by the law: *Items 7-11 of the liability page of the annual statement for life insurance companies, and items 16-19 and 26 of the liability page of the annual statement for miscellaneous stock companies, if a life insurance company is also transacting other kinds of insurance business.*** If other reserves are claimed, sufficient information must be filed with the return to enable the Commissioner to determine the validity of the claim. Reference should be made to the item in which the reserve appears in the annual statement and to the State statute or insurance department ruling requiring that such reserves be held. Only reserves which are so required, which are peculiar to insurance companies, and which are dependent upon interest earnings for their maintenance will be considered." (Italics ours.)

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*This provision has been incorporated in all regulations from 1921 to date.

**This provision was in the regulations from 1921 until Feb. 11, 1935 and not eliminated from the regulations applicable to the Acts of 1921, 1924, 1926, 1928 and 1932 until Dec. 15, 1935.

In all material respects, Art. 681 of Reg. 62 (1921 Act), Art. 681 of Reg. 65 (1924 Act) and Art. 681 of Reg. 69 (1926 Act) prior to amendment, as hereinafter referred to, were the same as Art. 971 of Reg. 74 (1928 Act) and Art. 971 of Reg. 77 (1932 Act), *supra*.

On February 11, 1935, Art. 203 (a) (2)-1 of Reg. 86 (1934 Act) was promulgated, which reads as follows:

> "In general, the reserve contemplated is a sum of money, variously computed or estimated, which, with accretions from interest, is set aside (reserved) as a fund with which to mature or liquidate, either by payment or reinsurance with other companies, future unaccrued and contingent claims. It must be required either by express statutory provisions or by rules and regulations of the insurance department of a State, Territory, or the District of Columbia when promulgated in the exercise of a power conferred by statute, but such requirement, without more, is not conclusive; for example, it does not include reserves required to be maintained to provide for the ordinary running expenses of a business definite in amount, and which must be currently paid by every company from its income if its business is to continue, such as taxes, salaries, reinsurance and unpaid brokerage; the reserve or net value of risks reinsured in other solvent companies to the extent of the reinsurance; reserve for premiums paid in advance; annual and deferred dividends; accrued but unsettled policy claims; losses incurred but unreported; liability on supplementary contracts not involving life contingencies; estimated value of future premiums which have been waived on policies after proof of total and permanent disability.
>
> "In any case where reserves are claimed, sufficient information must be filed with the return to enable the Commissioner to determine the validity of the claim. Reference should be made to the item in which the reserve appears in the annual statement and to the statute or insurance department ruling requiring that such reserves be held. Only reserves which are so required, which are peculiar to insurance companies, and which are dependent upon interest earnings for their maintenance will be considered. A company is per-

mitted to make use of the highest aggregate reserve called for by any State or Territory or the District of Columbia in which it transacts business, but the reserve must have been actually held.

"In the case of life insurance companies issuing policies covering life, health, and accident insurance combined in one policy issued on the weekly premium payment plan, continuing for life and not subject to cancellation, it is required that reserve funds thereon be based upon recognized tables of experience covering disability benefits of the kind contained in policies issued by this particular class of companies. The deduction in respect of such reserve funds (not required by law) is 3¾ per cent of the mean of such reserve funds held at the beginning and end of the taxable year."

Later the Commissioner promulgated Art. 203 (a) (2)-1 of Reg. 94 (1936 Act) and Art. 203 (a) (2)-1 of Reg. 101 (1938 Act), which articles were exactly the same as Art. 203 (a) (2)-1 of Reg. 86 (1934 Act), *supra*. It will be observed that Art. 203 (a) (2)-1 of Reg. 86 (1934 Act), 94 (1936 Act) and 101 (1938 Act) omitted the language which we italicized of Art. 971 of Reg. 74 (1928 Act) and Art. 971 of Reg. 77 (1932 Act), and which was also contained in Art. 681 of Reg. 62 (1921 Act), Art. 681 of Reg. 65 (1924 Act) and Art. 681 of Reg. 69 (1926 Act), *supra*. On December 18, 1935 the last-mentioned Regulations, namely, Art. 681 of Reg. 62 (1921 Act), 65 (1924 Act) and 69 (1926 Act), and Art. 971 of Reg. 74 (1928 Act) and Art. 971 of Reg. 77 (1932 Act) were amended by T. D. 4615 to read in all material respects the same as Art. 203 (a) (2)-1 of Reg. 86 (1934 Act), 94 (1936 Act) and 101 (1938 Act), omitting therefrom the italicized language referred to which was contained in said Regulations prior to amendment by T. D. 4615.

Attention is called to the fact that the provision regarding "reserve funds not required by law" as shown in boldfaced type above has been incorporated in all of the original and amended regulations from 1921 to the present time.